ST 03-0174-GIL 11/13/2003 USE TAX

This letter discusses tax issues for motor vehicles subject to either a true lease or conditional sale. See 86 Ill. Adm. Code 130.220 and 130.2010. (This is a GIL).

November 13, 2003

Dear Xxxxx:

This letter is in response to your letter dated August 11, 2003, in which you request information. The Department issues two types of letter rulings. Private Letter Rulings ("PLRs") are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department's regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter ("GIL") is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at www.ILTAX.com to review regulations, letter rulings and other types of information relevant to your inquiry.

The nature of your inquiry and the information you have provided require that we respond with a GIL. In your letter you have stated and made inquiry as follows:

> I am writing to request a written opinion on the application to your states Highway Use Tax (HUT), Rent Receipts Tax (RRT), Motor Vehicle Tax (MVT) or other applicable state sales, use or excise taxes on commercial motor vehicle lease transactions as outlined below. The relevant facts and our questions are as follows:
>
> Client name: NAME/OUT-OF-STATE ADDRESS
>
> Type of equipment: All Class A or Class B commercial
>
> Term of lease: Greater than 365 days to same person ('Long term lease')
>
> Issue (1): AAA acquires a commercial lease by purchase or assignment. The current user of the leased property is located in your state and the current lessor has paid the required 'up-front' tax on the vehicle or has begun remitting the alternative taxes. Receipts for the taxes paid are supplied to AAA at the time of the transaction. No changes are made to the lease document or terms, however the commercial vehicle is re-registered in the name of the new lessor, AAA*. A new lease is not signed. The vehicle user remains unchanged.
>
> Issue (2): Same as (1) except in this case AAA sells or assigns the lease. If titled, the title remains in the name of AAA.

Issue (3): A lease extension is formally documented with a lease extension <u>letter</u>, signed by both the lease assignee, if there is one, (or AAA if not) and the user. Nothing else changes.

Issue (4): A lease is sold by AAA or purchased by AAA. The transaction requires a new lease document (a re-writing and re-signing of the lease document). There is no change in the equipment covered by the lease, or the user of the equipment.

<u>Requested Rulings:</u>

Issue (1): No additional state taxes are payable.

Issue (2): No additional state taxes are payable.

Issue (3) This is not a new lease and is not subject to any additional state taxes

Issue (4) This is not a new lease (because the equipment and user do not change). Therefore the transaction is not subject to any additional state taxes

To date we have been unable to determine how your state would handle these matters and hope that you will be able to accommodate our request for a written opinion. If there are user fees applicable to this written request, please let me know and we will remit them.

Should you need more information please do not hesitate to contact me. Thank you for your assistance in this matter.

*If titled equipment, titled in the name of AAA, the equipment is domiciled in the state. For titled equipment the unit may or may not be titled and registered in your state for example if it is covered under IRP (International Registration Plan).

Illinois taxes the retail sale and use of tangible personal property under two separate but related statutes. The Retailers' Occupation Tax Act imposes a tax on Illinois retailers measured by a percentage of their gross receipts from sales for use or consumption. 35 ILCS 120/1 et seq. The Use Tax Act imposes a corresponding tax on purchasers by taxing the use of tangible personal property purchased from retailers. 35 ILCS 105/1 et seq.

In Illinois, lessors of tangible personal property under a true lease, except for automobiles leased for terms of one year or less, are considered to be the end users of the property to be leased. See 86 Ill. Adm. Code 130.220 and 130.2010. As the end users of tangible personal property located in Illinois, lessors incur Use Tax on the lessors' cost price of the property. Since lessors are considered the end users of the property and have paid the Use Tax, no Retailers' Occupation Tax is imposed upon the rental receipts and the lessees incur no Use Tax liability for the rental charges. In Illinois, a true lease generally has no buy out provision at the close of the lease. If a buy out provision does exist, it must be a fair market value buy out option in order to maintain the character of the true lease.

As stated above, lessees do not incur Use Tax liability in true lease situations. However, when a lessee registers the automobile, the lessee must either show that tax has been paid or that there exists an exemption from tax. If a lessee does not have documentation that the lessor has properly paid Illinois tax, the tax, as a practical matter, has to be paid by the lessee in order to register the vehicle since there is no exemption for leased vehicles. While lessees do not incur any tax liability in a true lease situation, it is typical of true leases to contain contractual provisions stating that the lessees will reimburse the lessors for their tax costs. This is not a matter of Illinois tax law but of private agreement between lessors and lessees. If the lessees agreed to such provisions, they are bound to satisfy that duty because of a contractual agreement, not because of Illinois tax law. Again, lessors are liable for Use Tax when they purchase vehicles for leasing purposes. However, lessors may have contractually required lessees to reimburse the lessors for the lessors' Use Tax that is incurred by the lessors in regard to the purchase of the leased vehicles.

The alternative to a true lease is a conditional sale. In Illinois, a conditional sale is usually characterized by a nominal purchase option at the close of the lease term. This type of transaction is considered a conditional sale at the outset of the transaction making all receipts subject to Retailers' Occupation Tax. See Section 130.2010. In this situation, lessors/retailers may give Certificates of Resale to their suppliers for tangible personal property transferred subject to a conditional sales agreement. The lessors/retailers owe Retailers' Occupation Tax on any installment payments when they are received by the lessors/retailers. The lessees/purchasers owe corresponding Use Tax on the amount of the installment payments that are collected by the lessors/retailers. However, tax on motor vehicles has to be paid up front at one time.

Section 10 of the Use Tax Act, 35 ILCS 105/10, provides that a purchaser of a motor vehicle from an out-of-State retailer shall file a return (Form RUT-25, Motor Vehicle Use Tax Return) with the Department and remit the proper amount of tax due on the selling price of the motor vehicle within 30 days after such motor vehicle is brought into this State for use. Assuming that an individual has entered into a true lease of a vehicle, the lessor is the purchaser who is required to file Form RUT-25 and remit the tax to the Department. Use Tax is properly due by the lessor when it purchases the vehicle for leasing purposes.

In a true lease situation, Illinois will give a credit for taxes properly due and paid in another state. See 86 Ill. Adm. Code 150.310. Depreciation is also allowed for out-of-State use. In addition, the Use Tax does not apply to the use, in this State, of tangible personal property which is acquired outside this State by a nonresident individual who then brings the property to this State for use here, and who shall have used the property outside this State for at least 3 months before bringing the property to this State. See 86 Ill. Adm. Code 150.315. This exemption is not applicable if the 3-month requirement is not met, or if the purchase is not made by a nonresident individual.

I hope this information is helpful. If you require additional information, please visit our website at www.ILTAX.com or contact the Department's Taxpayer Information Division at (217) 782-3336. If you are not under audit and you wish to obtain a binding PLR regarding your factual situation, please submit a request conforming to the requirements of 2 Ill. Adm. Code 1200.110 (b).

Very truly yours,

Martha P. Mote
Associate Counsel

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